

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 07-0300
Sales and Use Tax
For The Tax Years 2004-2005**

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ISSUES

I. Sales and Use Tax - Imposition.

Authority: IC 6-8.1-5-1(c); IC § 6-2.5-2-1; IC § 6-2.5-3-2(a); IC § 6-2.5-5-8(b);
Indiana Dep't of State Revenue v. Interstate Warehousing, 783 N.E.2d 248
(Ind. 2003).

The Taxpayer protests the imposition of adjusted gross income tax.

II. Tax Administration – Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2(b)(c).

The Taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

The Taxpayer is a corporation engaged in the excavation business. The Indiana Department of Revenue (Department) audited the Taxpayer for the tax years 2004-2005. The audit resulted in an assessment of additional use tax, interest, and penalty. The Taxpayer protested the assessment of use tax on a ditcher and penalty. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax - Imposition.

DISCUSSION

The Department assessed use tax on the Taxpayer's purchase and use of a ditcher in 2004. The Taxpayer protested the assessment arguing that it did not use the ditcher. Rather, the Taxpayer argued that it resold the ditcher. Therefore, according to the Taxpayer, the purchase of the ditcher qualified for the purchase for resale exemption from the sales and use tax.

All tax assessments are presumed to be valid. IC § 6-8.1-5-1(c). The Taxpayer bears the burden of proving that any assessment is incorrect. *Id.* Exemption statutes are to be strictly construed against the Taxpayer. *Indiana Dep't of State Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

IC § 6-2.5-2-1(a) imposes sales tax on retail transactions made in Indiana. IC § 6-2.5-3-2(a) imposes a complementary use tax on the storage, use or consumption of tangible personal property in Indiana, if the property was acquired in a retail transaction as defined for sales tax purposes. IC § 6-2.5-5-8(b) provides for an exemption for tangible personal property purchased to be resold in the Taxpayer's ordinary course of business.

45 IAC 2.2-5-15 clarifies the purchase for resale exemption as follows:

- (a) The state gross retail tax shall not apply to sales of any tangible personal property to a purchaser who purchases the same for the purpose of reselling, renting or leasing, in the regular course of the purchaser's business, such tangible personal property in the form in which it is sold to such purchaser.
- (b) General rule. Sales of tangible personal property for resale, rental or leasing are exempt from the tax if all of the following conditions are satisfied:
 - (1) the tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it;
 - (2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and
 - (3) The property is resold, rented or leased in the same form in which it was purchased.
- (c) Application of General rule.
 - (1) The tangible personal property must be sold to a purchaser who makes the purchase with the intention of reselling, renting or leasing the property. This exemption does not apply to purchasers who intend to consume or use the property or add value to the property through the rendering of services or performance of work with respect to the property.
 - (2) The purchaser must be occupationally engaged in reselling, renting or leasing such property in the regular course of his business. Occasional sales and sales by servicemen in the course of rendering services shall be conclusive evidence that the purchaser is not occupationally engaged in reselling the purchased property in the regular course of his business.
 - (3) The property must be resold, rented or leased in the same form in which it was purchased.

In 2004, the Taxpayer purchased the ditcher to use in its contracting business. Therefore, the sale of the ditcher was subject to the sales tax. The Taxpayer did not pay sales tax on the transaction. The Taxpayer used the ditcher once. The purchase of the ditcher was listed in the Taxpayer's books and accounts as the purchase of a capital asset. After the first trial use of the ditcher, the Taxpayer determined that the ditcher did not work in the manner intended by the Taxpayer. At that time, the Taxpayer decided to sell the ditcher. The Taxpayer did not sell the ditcher until 2005.

In the Taxpayer's case, there were two transactions. The first transaction was the Taxpayer's purchase of the ditcher. The second transaction was the Taxpayer's sale of the ditcher. The Taxpayer argued that the first transaction qualified for exemption as a purchase for resale.

To qualify for the "purchase for resale" exemption, the Taxpayer had to purchase the ditcher with the intention of reselling it. The Taxpayer tested the ditcher for use in digging drainage ditches. The Taxpayer also listed the ditcher as a capital asset. One can infer from these facts that at the time of purchase, the Taxpayer intended to use the ditcher to dig ditches. Therefore, the Taxpayer's purchase and use of the ditcher did not qualify for the "purchase for resale" exemption. The Department properly imposed use tax.

FINDING

The Taxpayer's protest is respectfully denied.

II. Tax Administration - Ten Percent Negligence Penalty.

DISCUSSION

The Taxpayer protests the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

The Taxpayer failed to pay the sales tax and use tax on many items that were subject to the tax such as miscellaneous supplies. This failure to follow the Department's directions and pay the appropriate tax liabilities constitutes negligence.

FINDING

The Taxpayer's protest to the imposition of the penalty is respectfully denied.